# R.J.Reynolds Industries, Inc., 1975 Annual Report

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# HIGHLIGHTS

(Dollar Amounts in Thousands Except Per Share Statistics)

| | 1975 | 1974 | Change |
|---|---|---|---|
| FOR THE YEAR | | | |
| Net sales and revenues | **$4,837,643** | $4,500,909 | + 7.5% |
| Net earnings | **338,673** | 296,903 | + 14.1% |
| Net earnings per common share: | | | |
| Primary | **7.39** | 6.66 | + 11.0% |
| Fully diluted | **6.71** | 5.97 | + 12.4% |
| Net earnings as a percentage of net sales and revenues | **7.0%** | 6.6% | |
| Return on average total capital | **15.2%** | 14.8% | |
| Return on average common stockholders' equity | **19.0%** | 18.7% | |
| Capital expenditures | **$ 174,639** | $ 125,832 | + 38.8% |
| AT YEAR END | | | |
| Working capital | **$ 983,673** | $ 823,507 | + 19.4% |
| Book value per common share | **40.68** | 37.40 | + 8.8% |
| Number of stockholders | **121,398** | 125,176 | - 3.0% |
| Number of employees | **34,666** | 32,454 | + 6.8% |

The financial information for 1974 has been restated to reflect a change in method of accounting for foreign currency translation. See Note A to the financial statements.

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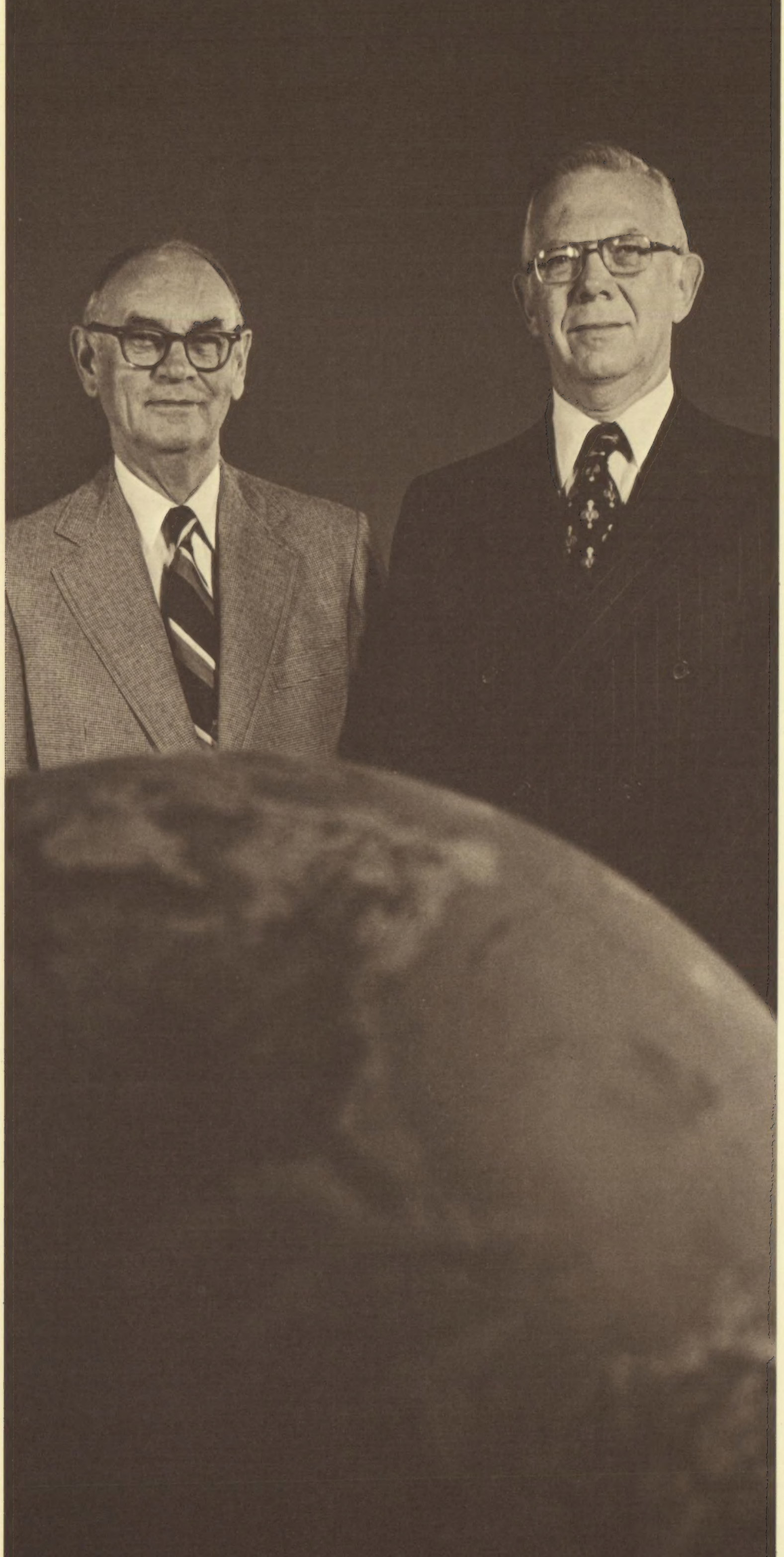


# LETTER TO STOCKHOLDERS

**Dear Stockholders:**

It is a pleasure to report to you that 1975 was another record year for your Company. New highs were achieved in sales and revenues and net earnings.

All of us are especially pleased that 1975 was such a good year, following 1974 and 1973 which were also new record performances for your Company, when all three of those years were tough times in the economy generally.

Marked sales improvement in our tobacco business and record performance from our foods subsidiary helped overcome general weakness in the international economy affecting some of our other operations.

The record results for 1975 showed consolidated sales and revenues up 7.5 percent from 1974 and net earnings up 14 percent. Fully diluted earnings per common share were $6.71, an increase of 74 cents over the 1974 figure. (Prior-year amounts have been restated to reflect an accounting change, discussed in the financial review which begins on page 16.)

At its October meeting the Board of Directors voted to raise the quarterly dividend on the Common Stock to 77 cents per share, an increase of 5 cents over the amount paid in the previous four quarters. The Company's dividend payment per common share has increased each year for the past 22 years except for 1971, when dividend increases were prohibited by Federal economic guidelines. Last year was the 76th consecutive year of dividend payments.

In the last annual report we told you that your Company's opportunities and activities in the international field were growing, and that we were forming an International Advisory Board to avail ourselves of the advice and guidance of people in positions of leadership in other countries. In the first year of its existence we have found this new board of great value. The organizational meeting was held here in Winston-Salem in May, and the second meeting took place in Geneva in November. In their advisory capacity to your Board of Directors, these eminent businessmen and industrialists from various parts of the world are proving quite helpful as we continue to develop our guidelines for policies and operations outside the United States.

Indicative of your Company's growth internationally is the formation of a new subsidiary, R.J.Reynolds Tobacco International, Inc., to direct our international tobacco activities. We will tell you more about it later in this letter.

While our Company is involved in several different businesses, there is a common tie that binds the total corporation together. From its early days on through the centennial year it has just celebrated, R.J.Reynolds Tobacco Company has always been an outstanding example of *marketing* success. With our entry into other businesses — aluminum products and packaging, food and beverage products, international petroleum and containerized freight transportation — the Reynolds organization has applied its unique marketing savvy with corresponding success to a wide variety of goods and services.

Whether you are selling consumer products, services, industrial products, creative ideas or whatever, the marketing techniques are essentially the same. Moreover, when you put good products and services together with good marketing skills, you are going to come out on top — and that is precisely what we attempt to do. We believe that we have fine products and services plus the know-how to sell them.

From subsidiary to subsidiary, our production facilities and techniques differ widely, but marketing the end products of each requires the same abilities. And it is truly the marketing mastery of our people, wherever situated, that is the tie which binds the elements of our far-ranging Company together.

The operational activities of our Company's subsidiaries during 1975—our centennial year—were

Colin Stokes, Chairman (left), and J. Paul Sticht, President.

**Wm. D. Hobbs, Chairman and President**

## R.J.Reynolds Tobacco Company

R.J.Reynolds Tobacco Company is the nation's leading cigarette manufacturer with sales totaling nearly one-third of the domestic market. Six of the company's brands—WINSTON, SALEM, CAMEL, VANTAGE, DORAL and MORE—are ranked in the top 25 brands in the U.S. The company also manufactures the nation's leading smoking tobacco, plug chewing tobacco and little cigar.

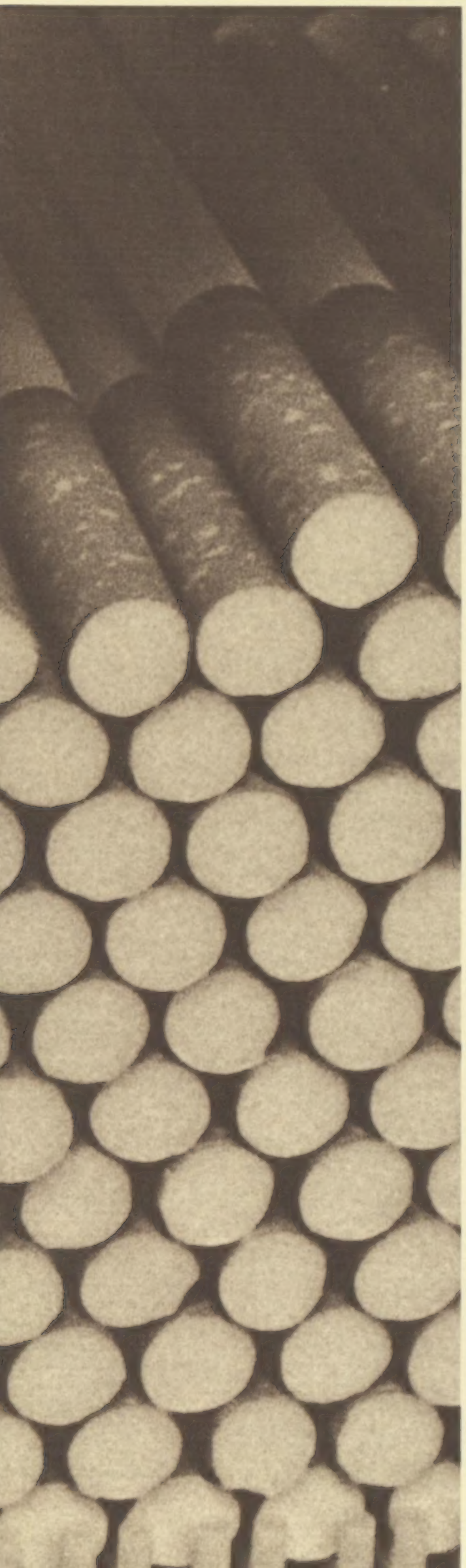
most gratifying. During a continued uncertain economic climate, the subsidiaries proved they had the flexibility and the strength to capitalize on opportunities.

**Appropriately, R.J.Reynolds Tobacco Company closed its 100th year of business by reporting record sales and earnings and strengthening its leadership of the domestic cigarette market.**

Reynolds Tobacco increased its share of the U. S. cigarette market almost one percentage point to about one-third of the market, marking its greatest market-share increase since 1962. Of equal significance, the company's leading brand, WINSTON, after three years of static performance, increased its sales during the year and retained its number one position in the market for the tenth consecutive year.

In all, Reynolds Tobacco placed six brands among the nation's top 25 best-selling cigarettes. SALEM and CAMEL, two of the company's established brands, moved up one place each to fourth and sixth places, respectively, and VANTAGE, MORE and DORAL, all more recent entries, helped strengthen the company's overall position in the marketplace.

VANTAGE continued its climb and grew at a rate of 28.3 percent during the year and rose to 12th position. MORE—the 120mm brand with which Reynolds Tobacco introduced an entirely new cigarette category—went into national distribution early in the year and captured almost 1 percent of the



market. The brand's outstanding performance was enough to establish MORE as the nation's 25th best-selling brand.

DORAL, the company's other entry in the low "tar" and nicotine category, remained in 20th position among the leading brands.

**The diversity of the leading brands Reynolds Tobacco offers smokers and the success of the brands are indicative of our tobacco company's marketing philosophy. We try to anticipate shifts in smoker preferences and introduce brands to meet consumer tastes before anyone else does. Regardless of changes in smoker tastes, our tobacco company is determined to have a leading brand in every cigarette category.**

In keeping with this philosophy, new brand development continued during 1975, despite the impressive lineup of successful brands the company already has on the market.

SALEM Lights, a lower "tar" and nicotine version of the already popular SALEM brand, went into national distribution in November and has generated encouraging initial response.

The low "tar" and nicotine category has been growing at a rapid rate, led by our own VANTAGE brand. However, market research has shown indications of a growing demand among some smokers for even lower "tar" and nicotine than those of the already popular brands.

To meet this increasing demand, Reynolds Tobacco introduced its new NOW brand just before the end of the year. At year end NOW had the lowest "tar" and nicotine levels of all king-size cigarettes on the market, with only 2 mgs. of "tar" and 0.2 mgs. of nicotine. Achieving these levels meant a reduction of 50 percent in "tar" and 33 percent in nicotine compared to the previously lowest king-size brand on the market. Yet our tobacco company team met this goal without sacrificing the new brand's pleasant taste.

In addition to concentrating on its brand activity, Reynolds Tobacco devoted considerable attention during the year to improving its position in the major metropolitan markets of the country. Despite its position of leadership in the national cigarette market, Reynolds Tobacco felt its sales levels in some metropolitan areas could be strengthened. To begin working toward this goal, the company launched special market development programs in key metropolitan areas. The market development programs were supported by the full resources of the company. As a result, Reynolds Tobacco's growth rate in the nation's top three cities during 1975 exceeded the company's overall share-of-market increase.

Although cigarettes are R.J.Reynolds' primary tobacco product, there are other products which contribute to its leadership in the U.S. tobacco industry. PRINCE ALBERT remained the nation's leading smoking tobacco in 1975, and DAYS WORK was once again the best-selling plug chewing tobacco.

In addition to all our activities aimed at increasing our market

leadership in the U.S. tobacco industry during 1975, we have continued our commitment, begun in 1954, to The Council for Tobacco Research—U.S.A., Inc., which makes grants to independent scientists for research on matters related to tobacco and health. This year's budget attributable to research, which is also supported by others in the tobacco industry, comprises $5.9 million.

At Harvard Medical School we and others in the tobacco industry are supporting research on questions of tobacco and health through a five-year grant in the total amount of $2.5 million.

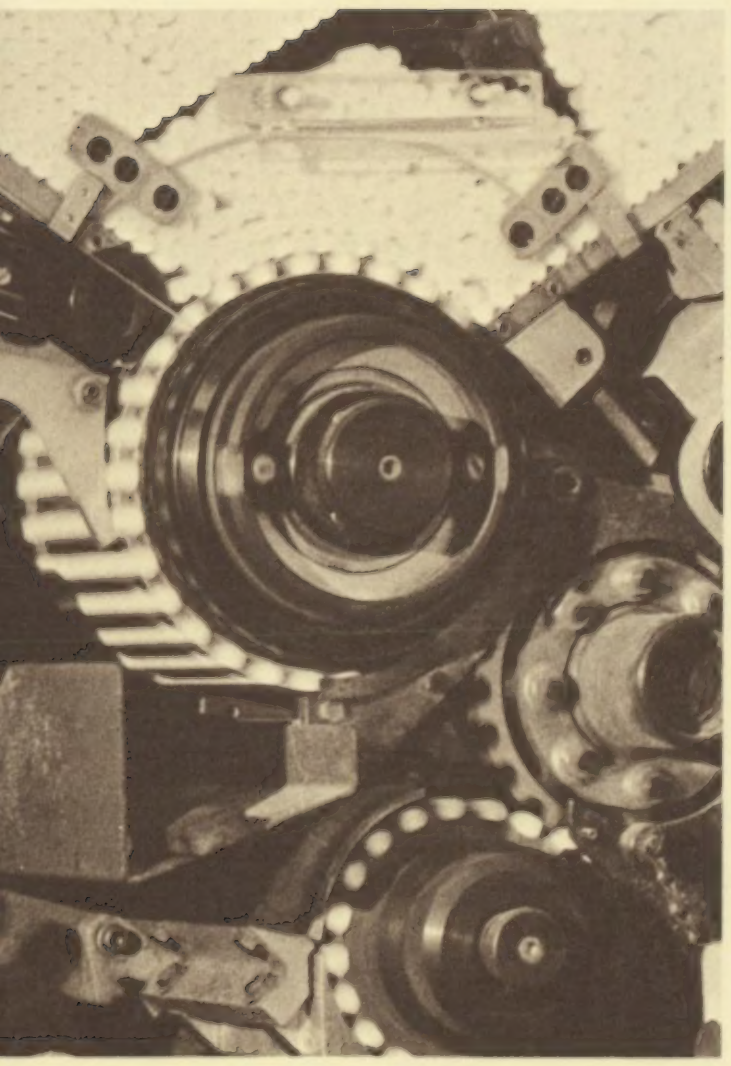
Other major research projects supported by your Company include a five-year, $1.7 million research program at UCLA on lung defense mechanisms and early detection and treatment of cancer; and a basic research program on the immunologic properties of cancer at Washington University in St. Louis on which the tobacco industry has spent or committed $2.8 million.

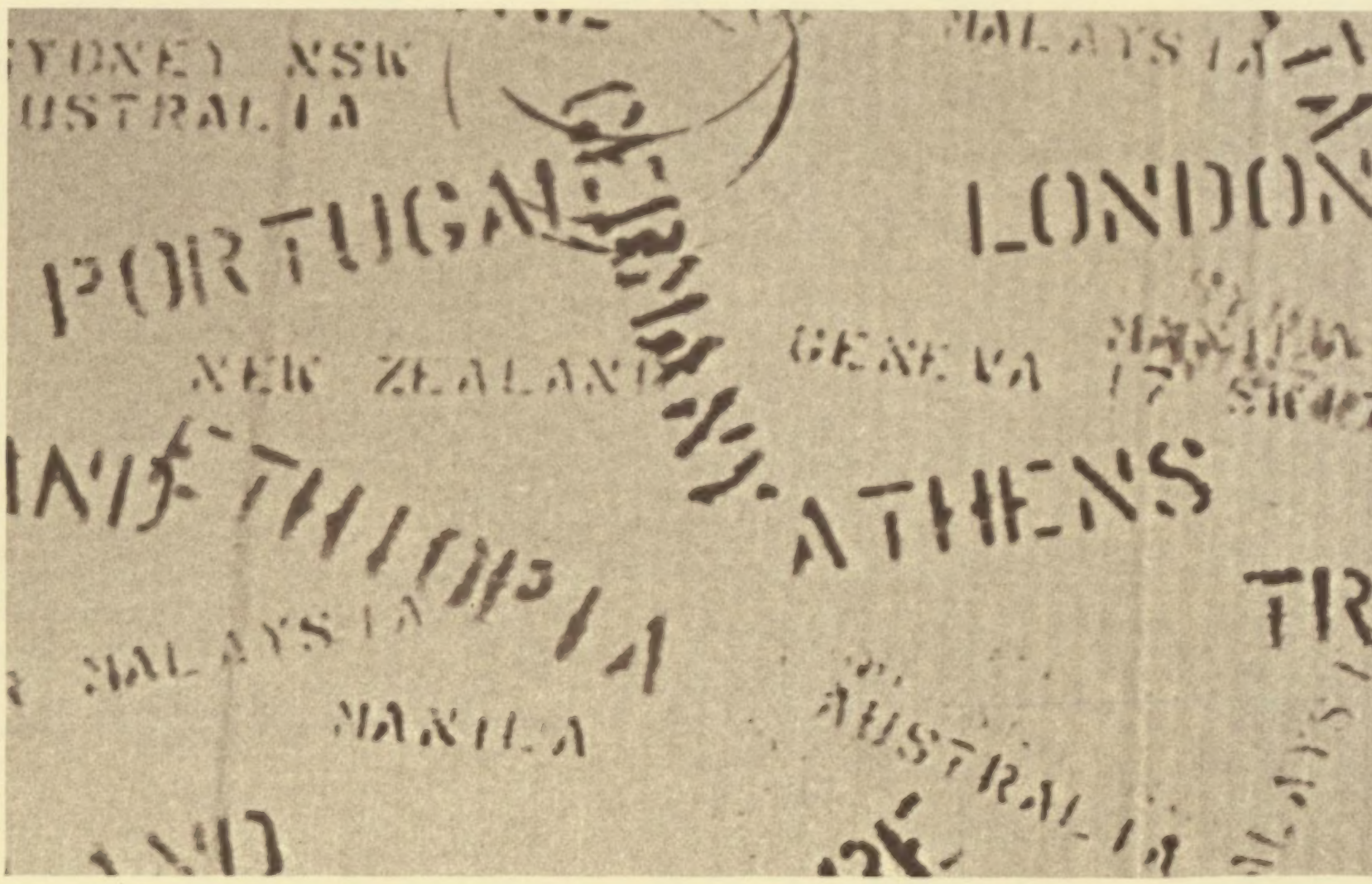
**However, all of our corporate research grants are not restricted to the question of smoking and health. We are firmly committed to the support of medical research in general. It is only through the work of competent scientists that the principal diseases now afflicting mankind can be understood and conquered. Last year we made a pledge of $2.8 million to The Rockefeller University.**

This amount is payable over a five-year period for basic research, clinical investigation and advanced education in the biomedical sciences, and for the endowment of a postdoctoral fellowship in the biomedical sciences. The grant will benefit a wide range of fundamental research programs and clinical investigations required to develop improved methods for treating and preventing conditions such as cancer, degenerative diseases and genetic disorders.

For the past 50 years, the tobacco industry and American smokers have borne the burden of ever-increasing cigarette taxes levied by states and municipalities. Regressive taxes place an unreasonable financial burden on smokers, result in lost sales adversely affecting millions of people connected with the tobacco industry and create profits for organized crime.

In many cases, such taxes are the result of activities by anti-smoking





**J. Tylee Wilson, President**

## R.J.Reynolds Tobacco International, Inc.

International tobacco operations outside the United States are directed by R.J.Reynolds Tobacco International, Inc., headquartered in Winston-Salem. Through its subsidiaries and licensees, the company has local manufacturing facilities in more than 20 countries, providing the foundation for marketing RJR cigarette brands in more than 140 countries.

groups seeking to damage or destroy the tobacco industry. In addition to supporting exorbitant cigarette taxation, these groups attempt to use against the industry such issues as the allegedly harmful effects suffered by non-smokers exposed to cigarette smoke. Despite studies by institutions such as Harvard University School of Public Health which have shown there is no basis for such claims, regulations against smoking in public places are being enacted with increasing frequency.

R.J.Reynolds will continue to work with the Tobacco Institute and the Tobacco Tax Council to make the true facts about all issues of smoking and health known and to oppose further regressive cigarette tax increases.

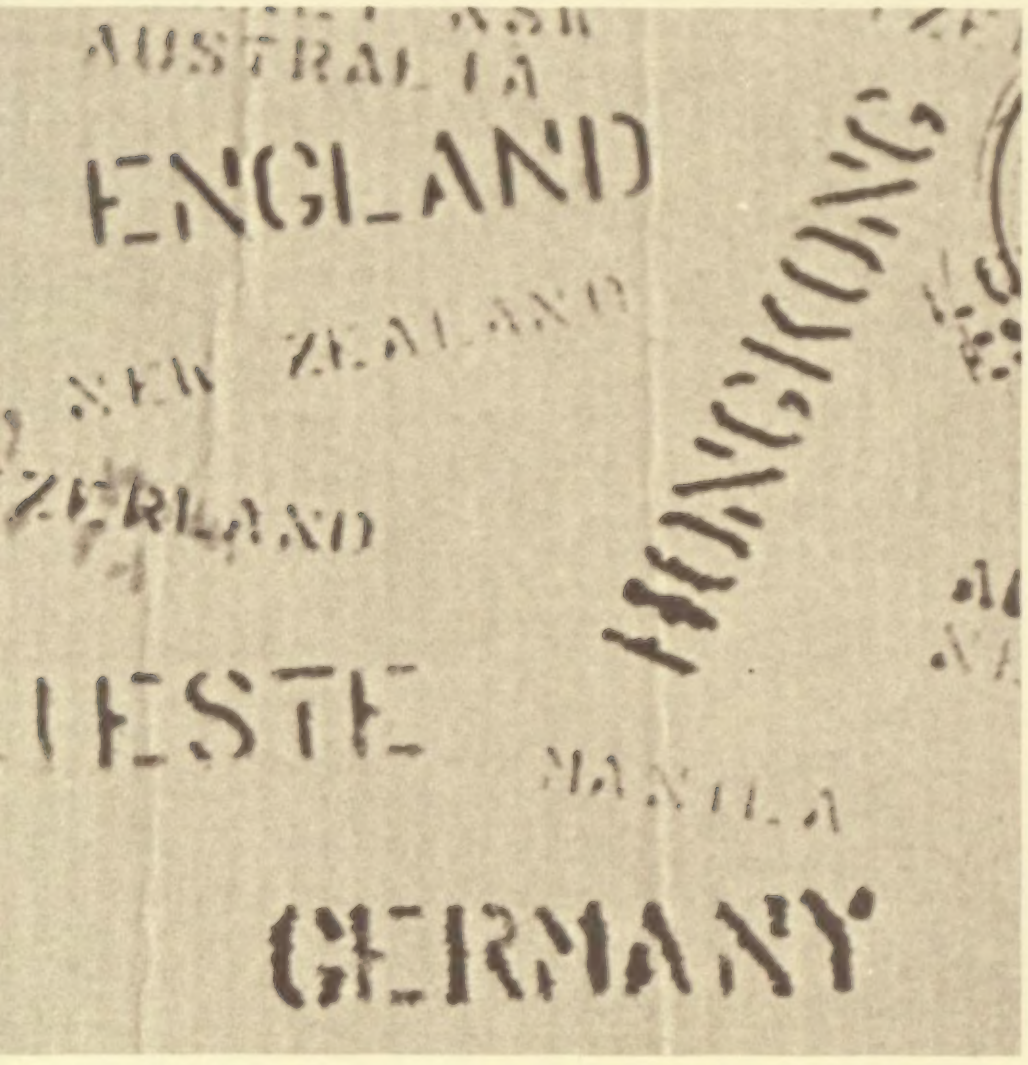
While the tobacco company is our first and oldest member of the corporate family, we are pleased that it has retained an aggressive and vigorous approach in its efforts. These qualities, combined with the benefits of the stability and maturity the company has gained by being so long an industry leader, enhance its prospects for the future.

**It became apparent during 1975 that our growth in the international tobacco market was such that we needed consolidated overall management for these activities. Accordingly, plans were completed in December to form a new subsidiary, R.J.Reynolds Tobacco International, Inc., to be headquartered in Winston-Salem and to be responsible for our Company's international tobacco operations.**

Our international growth record in recent years, coupled with the centralized international management, will enable our Company to make continued strides in the world market. Having the international headquarters in Winston-Salem will help us apply to the world market the technical, marketing and management know-how that have made R.J.Reynolds the leader in the U.S. market.

During 1975, we continued our concerted effort to expand our international tobacco activities and further capitalize on the growth potential of the world market.

Total unit cigarette consumption outside the U. S. last year was over 3 trillion, 600 billion, more than six times the size of the U. S. market. The growth rate in the international



**Michael R. McEvoy, Chairman**
**Charles I. Hiltzheimer, President**

## Sea-Land Service, Inc.

Sea-Land Service, Inc. is the world's largest containerized freight transportation company and the originator of the revolutionary land-ocean transportation concept. Sea-Land serves 133 ports around the world with more than 62,000 special containers and a fleet of 66 vessels. The company's fleet includes eight SL-7 super containerships which provide the fastest containerized shipping service in the world.

area also exceeded that of the domestic market, a trend we expect to continue.

**To strengthen our ability to take advantage of the opportunities available abroad, we signed licensing agreements during 1975 with manufacturers in three additional countries. We also signed a technical assistance agreement with the U.S.S.R., and acquired substantially all the manufacturing and distribution assets of a Brazilian manufacturer in 1975.**

In July, R.J.Reynolds became the first cigarette manufacturer to sign a licensing agreement involving tobacco and tobacco products with Bulgartabac, the Bulgarian state-owned tobacco corporation. Under the terms of the agreement Bulgartabac was ready to begin manufacture and distribution of WINSTON by the end of the year.

Our three leading U.S. brands—WINSTON, SALEM and CAMEL—will be manufactured in New Zealand under an agreement completed in November with Rothmans, New Zealand Ltd. CAMEL Filter, one of the most popular R.J.Reynolds products sold in foreign countries, is being produced in Finland by P. C. Rettig & Company, through a licensing agreement.

Representatives of our Company and the State Committee of the U.S.S.R. Council of Ministers for Science and Agriculture met in Moscow in July to sign a long-term agreement covering various aspects of the tobacco and cigarette fields. A protocol relative to tobacco growing, harvesting and processing was also signed.

The principal objective of both agreements is to expand production and improve the quality of tobacco and cigarettes in the Soviet Union on a cooperative basis. Meetings between technical experts representing all parties are planned to determine further details of the agreements.

**Another of the key growth potential markets of the world is South America. In 1974 we established a foothold in Brazil by forming R.J.Reynolds Tabacos do Brasil Ltda. Last year we found an opportunity to strengthen our position in this market, and, through R.J.Reynolds Tabacos do Brasil, acquired the manufacturing and distribution assets of Cia. Lopes Sa Industrial de Fumos.**

Lopes Sa manufactures 14 principal cigarette brands for distribution in Brazil with annual sales volume of approximately 8 billion units. The acquisition is expected to give our Company approximately 12 percent of the growing Brazilian cigarette market.

Our total international unit sales increased more than 16 percent during 1975, with the largest gains concentrated in the Middle East and Latin America.

Unit sales of our domestic brands exported to foreign countries were also up substantially for the year. An overall 16 percent increase was led by an 18 percent growth in unit sales of exported WINSTON, and boosted by the introduction of MORE into the export market. At year end, MORE was being exported to Asia, Australia, Latin America and Europe, and was experiencing rapidly increasing popularity in each market.

Macdonald Tobacco Inc., our Company's Canadian tobacco subsidiary, also contributed to R.J.Reynolds' worldwide success in 1975. The Canadian company doubled its earnings from operations from the previous year, and slowed its recent decline in share of market.

Macdonald's EXPORT "A" remained Canada's best-selling cigarette, and two brands, CAVALIER and MORE, were successfully introduced nationally. VANTAGE was introduced into test markets in Canada, and by the end of the year had captured a 1.6 percent share of market in its test areas.

In order to centralize Macdonald's cigar manufacturing operations, all cigar operations were consolidated in Montreal and its cigar production plant in Toronto was sold. Macdonald also purchased during the year the assets of Simon Cigar Company, Canada's second-largest cigar manufacturer.

R.J.Reynolds brands are now sold in more than 140 countries, with local manufacturing in more than 20 countries.

**Throughout our corporation we are striving to assure that our products and services represent the utmost in quality and**

**dependability. We feel that the company which maintains these characteristics at the highest level will be the last to feel the pinch during economic slumps and the first to broaden its market share during economic gains. This is especially true in the shipping industry.**

Since our Company acquired Sea-Land in 1969, we have devoted considerable time and expense to make this company the leader in the international containerized shipping industry. We feel this effort is paying dividends. The flexibility and quality inherent in Sea-Land's new fleet, which includes the SL-7 container-ships, and its network of shore facilities enabled Sea-Land to make significant improvements in the quality of its service and cargo during 1975 even though world trade volume was off overall.

**With its network of vessels fully deployed during the year, Sea-Land fared better in the Pacific last year—generally conceded to be an off year—than it did in 1974, which was a better year for the industry.**

Declines in the company's domestic routes, however, including seasonal declines in the Alaskan service, more than offset revenue improvement.

Based on early economic indicators, Sea-Land redeployed a number of its 66-vessel fleet during 1975 and achieved optimum utilization, especially considering world trade factors.

Midway through the year Sea-Land inaugurated three sailings per

**J. B. Sunderland, President**

## American Independent Oil Company (Aminoil)

Aminoil is an international independent petroleum producer and refiner selling primarily to other oil companies. Although Aminoil's principal sources of oil are in the Middle East and its refinery and desulfurization plant are in Kuwait, it is exploring for new oil and natural gas sources in the United States and overseas.

week to Alaska. To meet the growing commercial needs of this northern state, the company also increased its service to the Aleutian chain to support the fishing industry of this region.

The Caribbean service was strengthened by the direct calls of a Sea-Land vessel at the new container facility in Kingston, Jamaica, thus giving the company another link, along with San Juan, from which it can serve Caribbean markets.

In Europe, Sea-Land added Bilbao, Spain, and Koper, Yugoslavia, to its network of ports served, and centralized its Mediterranean operations at the port of Algeciras, Spain, where it has room for greater expansion than at Cadiz where operations were located previously.

On the domestic scene, Sea-Land and the city of Portsmouth dedicated a new multi-million-dollar terminal in that Virginia city to better serve the area's shippers and consignees.

In the past ten years, Sea-Land has grown from a modest-sized company with 13,535 containers, 15 containerships and service to 15 ports to become the world's largest containerized freight organization. Today Sea-Land has more than 62,000 containers and a fleet of 66 ships that serve 133 ports around the world.

**This rapid growth has brought about steady, calculated changes throughout the company. During last year, Sea-Land was reorganized to make the best use of its managerial resources.**

Overall, much of the activity of Sea-Land during 1975 served not only to add to the company's performance last year, but also to prepare the company to capitalize on opportunities anticipated as world trade improves in future years.

**Almost universally the petroleum industry was faced with a reduced level of consumption of crude oil products during 1975 with almost worldwide oversupply. However, crude oil prices held relatively firm as a result of policies set by the Organization of Petroleum Exporting Countries (OPEC).**

Aminoil's largest volume product is fuel oil, for which demand was particularly depressed as a result of

**Robert L. Remke, President**

## RJR Foods, Inc.

Supermarkets across the nation and in Canada carry convenience food products and beverages produced by RJR Foods, Inc. Three of the company's most famous brands are HAWAIIAN PUNCH, one of the leading fruit drinks, CHUN KING Oriental foods and PATIO Mexican foods.

the continuing recession in major industrial nations. However, Aminoil has a long-established fuel oil supply position east of Suez and shipments for this area remained at a high level.

During 1975, Aminoil shipped approximately 72,000 barrels of products per day from Kuwait and more than 47,000 barrels daily from its interest in Iran.

Aminoil continued efforts to diversify its sources of petroleum supplies during 1975 and accelerated its exploration and production activities in the United States. As a part of its expanding search for domestic energy sources, Aminoil participated in the exploration or development of 20 Federal leases in the offshore area of the Gulf of Mexico.

**From one of these sites Aminoil, as a partner with other companies, will soon begin producing and selling natural gas. Additional leases are scheduled to begin production during the 1976-77 period.**

Another highlight of the 1975 exploration program came in December when Aminoil was a participant in successful groups which were awarded five offshore leases in the recent Federal sale in California.

In non-domestic exploration activities, Aminoil participated in an offshore drilling program in Spain which resulted in a non-productive well. Additional geological evaluations were being made at the end of the year to determine if further drilling was warranted.

Later in the year, Aminoil Indonesia, Inc., and its partners made arrangements to convey half of their interest in an Indonesian production contract to another company in exchange for the drilling of two wells.

To handle ongoing and proposed expansion plans in exploration, production and marketing, Aminoil was completing plans by the end of the year to expand its personnel and facilities in New York and Houston.

**Last year was a record year for RJR Foods in terms of sales and earnings from operations despite consumer pressure on the convenience foods industry due to the economic recession.**

One of the most significant achievements of the year for our

foods company was the progress it made in share-of-market gain for its largest-selling brand, HAWAIIAN PUNCH, during an off year for the general market. HAWAIIAN PUNCH posted an all-time-high market share in the fruit drink category, and the brand's Fruit Juicy Red continued to be the best-selling flavor.

**The year was also one of new product thrust. Two new items were introduced in the PATIO line and three in frozen CHUN KING. Low Sugar HAWAIIAN PUNCH was introduced nationally in June, and 64-ounce HAWAIIAN PUNCH in a glass container was introduced in October. HAWAIIAN PUNCH powdered drink mix was test marketed and will be launched nationally in 1976.**

In addition to significant new product activity, our foods company also moved ahead with its program to improve facilities and staff.

A new 205,000-square-foot manufacturing and distribution facility in South Brunswick, New Jersey, opened on schedule in November. HAWAIIAN PUNCH fruit drinks and VERMONT MAID syrup will be produced in the new plant. The plant will also serve as a distribution center for other RJR Foods products to the northeastern part of the nation.

**J. H. Corrigan, Jr., President**

## RJR Archer, Inc.

RJR Archer, Inc. is a leading producer of specialty foil and sheet aluminum products, packaging materials, gift wrap, bows and ribbons, and protective film wrap. Archer products are used for packaging many of America's best-known consumer goods, and the company produces household foil and gift wrap for major department stores and other private-label retail outlets.

During the year, the foods company started construction of a production and distribution facility in Atlanta. When completed in mid-1976, the facility will make HAWAIIAN PUNCH and become the main distribution point in the southeast for the company's non-frozen food products.

In September, RJR Foods completed a major management restructuring program which began a year earlier. We feel the company is now properly organized to take full advantage of opportunities in its highly competitive industry.

**Despite a slow start due to the generally unfavorable economic factors at the beginning of 1975, RJR Archer ended the year with a heavy backlog of orders.**

Many of Archer's customers operated from their own inventories early in 1975 as they waited for clear indications as to which way the economy would move for the year. Consequently, some Archer plants were forced to cut back to four-day schedules. But by August, they were all back in normal production. In fact, by the latter part of the year the Metals Division, the Packaging Division and Filmco were working overtime.

The Metals Division experienced reduced demand because many of its products ultimately go into the building trades. While no immediate turnaround in the construction industry appears imminent, there are signs that concern over energy consumption will bring about greater utilization of aluminum products in areas where weight is a significant factor.

Work continued during the year on the $13 million continuous aluminum casting facility at Huntingdon, Tennessee, which is scheduled to start operation in the summer of 1976. The new facility will add 62 million pounds annually to the Metals Division's total aluminum casting capacity and provide greater flexibility in usage of raw materials, including pig, scrap and molten aluminum.

Design of the 80-inch and 66-inch casters being installed will provide improved efficiency by permitting production of increased widths and thicknesses and greater casting speeds. Quality will also be improved by a molten metal filtration system. The total system includes the most advanced pollution controls.

The 80-inch caster is unique in the aluminum industry. The "super caster," which is 14 inches larger than the biggest now in use, will operate about 50 percent faster than present casters and give Huntingdon the capacity to cast half-inch thicknesses of coiled sheet aluminum.

The flexible packaging industry, in which Archer plays a key role, saw its production double during the past five years and it is forecasting a 100 percent gain in the next five years. More and more products are going into flexible packaging canisters and pouches, thus offering Archer considerable potential in this area.

Archer's Artistic/Consumer Division, which produces a wide range of giftwrapping products, reported a

slow buying season in the spring of 1975 but at the end of the year anticipated a heavier surge for the coming season due to increased consumer confidence.

We feel that pride in our Company's performance during 1975 and optimism concerning our future are appropriately justified. The Company's much-deserved reputation for dependability helped assure continued loyalty from its long-term customers. Our Company today is vastly different from the plug chewing tobacco company started by our founder, Richard Joshua Reynolds, in 1875. The R.J.Reynolds Industries of the future will one day be vastly different from the one we are reporting on for last year. While we have changed to meet contemporary demands, we think we have been consistent in demonstrating a gratifying record of success.

**This success over the years has been due to the joint efforts of our employees around the world, the confidence placed in our Company by our shareholders and our mutually satisfying relationships with suppliers and customers.**

**For all of this, we are grateful.**

*Respectfully submitted for the Board of Directors,*

Colin Stokes
Chairman, Board of Directors

J. Paul Sticht
President

February 12, 1976

# FINANCIAL REPORT

# FIVE-YEAR CONSOLIDATED SUMMARY OF OPERATIONS

(Dollar Amounts in Thousands Except Per Share Statistics)

| | 1975 | 1974 | 1973 | 1972 | 1971 |
|---|---|---|---|---|---|
| **Net sales and revenues:** | | | | | |
| Tobacco | **$3,321,454** | $2,895,763 | $2,349,617 | $2,168,242 | $2,084,938 |
| Transportation | **768,068** | 854,780 | 582,631 | 450,886 | 360,656 |
| Petroleum | **440,369** | 461,223 | 99,989 | 78,308 | 71,937 |
| Other | **307,752** | 289,143 | 262,676 | 260,194 | 271,449 |
| Total | **$4,837,643** | $4,500,909 | $3,294,913 | $2,957,630 | $2,788,980 |
| **Earnings from operations:** | | | | | |
| Tobacco | **$ 528,063** | $ 412,585 | $ 434,227 | $ 404,487 | $ 450,683 |
| Transportation | **89,684** | 143,169 | 17,211 | 31,722 | 18,242 |
| Petroleum | **194,645** | 254,072 | 51,909 | 35,679 | 25,687 |
| Other | **30,079** | 15,402 | 22,139 | 16,810 | 19,444 |
| Total | **842,471** | 825,228 | 525,486 | 488,698 | 514,056 |
| Interest and debt expense | **54,465** | 57,598 | 40,602 | 30,169 | 29,694 |
| Foreign currency (gains) losses | **(15,514)** | 28,590 | 28,795 | 1,086 | 7,952 |
| Other (income) expense, net | **(13,720)** | (14,246) | (8,609) | (7,767) | (6,650) |
| Earnings before provision for income taxes | **817,240** | 753,286 | 464,698 | 465,210 | 483,060 |
| Provision for income taxes | **478,567** | 456,383 | 218,427 | 234,490 | 259,087 |
| **Net earnings** | **338,673** | 296,903 | 246,271 | 230,720 | 223,973 |
| Less preferred dividends | **12,129** | 15,772 | 15,906 | 16,580 | 17,346 |
| Net earnings applicable to Common Stock | **$ 326,544** | $ 281,131 | $ 230,365 | $ 214,140 | $ 206,627 |
| **Net earnings per common share:** | | | | | |
| Primary | **$7.39** | $6.66 | $5.48 | $5.15 | $5.05 |
| Fully diluted | **6.71** | 5.97 | 4.99 | 4.60 | 4.50 |
| **Average number of common shares outstanding:** | | | | | |
| Primary | **44,183,793** | 42,188,574 | 42,064,408 | 41,547,108 | 40,907,239 |
| Fully diluted | **50,473,159** | 49,765,082 | 49,321,395 | 50,140,565 | 49,780,139 |

Certain accounts for 1974 and prior years have been restated to reflect a change in method of accounting for foreign currency translation. See Note A to the financial statements.

## SALES AND EARNINGS

Consolidated net sales and revenues for 1975 were a record $4.8 billion, up $337 million, or 7.5%, over the 1974 amount. Net earnings in 1975 increased $42 million, or 14%, over 1974 to a record $339 million. Fully diluted net earnings per common share increased 74 cents to $6.71 in 1975. (Primary earnings per common share increased 73 cents over 1974 to $7.39.)

During the fourth quarter of 1975, the Company changed its method of accounting for foreign currency translation as required by Statement No. 8 published by the Financial Accounting Standards Board (FASB) in October, 1975. Financial statements for 1974 and prior years have been restated to reflect this change.

The impact of this new requirement has been to include in the Company's financial statements substantial foreign currency translation gains and losses which may not be ultimately realized and which may reverse in future periods causing potentially material increases or decreases in earnings. For this reason the Company opposed the adoption of this requirement by the FASB. Prior to this new requirement, it had been the Company's policy to recognize foreign currency gains and losses associated with long-term receivables and payables only when realized in cash.

The accounting change increased (decreased) earnings from operations and net earnings for the five years ended December 31, 1975, as shown in the following table:

(Dollars in Thousands Except Per Share Statistics)

| | Earnings From Operations | Net Earnings | Net Earnings Per Common Share Primary | Net Earnings Per Common Share Fully Diluted |
|---|---|---|---|---|
| **1975** | | | | |
| First quarter | $ 346 | $ (4,038) | $(.09) | $(.08) |
| Second quarter | 346 | 1,693 | .04 | .03 |
| Third quarter | 346 | 16,530 | .37 | .33 |
| Fourth quarter | 351 | (3,565) | (.08) | (.07) |
| **Total 1975** | **1,389** | **10,620** | **.24** | **.21** |
| 1974 | 1,387 | (13,795) | (.33) | (.27) |
| 1973 | 676 | (17,298) | (.41) | (.35) |
| 1972 | 34 | (601) | (.02) | (.01) |
| 1971 | — | (5,092) | (.13) | (.10) |

Additional information regarding this accounting change is included in Note A to the financial statements.

In 1974, the Company's net sales and revenues and restated net earnings show increases of $1.2 billion, or 37%, and $51 million, or 21%, respectively, over 1973. Restated fully diluted earnings per common share in 1974 were $5.97, 20% greater than in the prior year. (Restated primary earnings per common share were $6.66 in 1974, an increase of 22% over 1973.)

Over the past five years, net sales and revenues and net earnings have increased at average annual compound rates of 13% and 10%, respectively.

Consolidated earnings from operations increased $17 million in 1975 and $300 million, or 57%, in 1974 compared with the preceding year. (Earnings from operations are earnings before interest and debt expense, foreign currency gains and losses, other income and expense, and provision for income taxes.) Approximately two-thirds of the 1974 increase resulted from the petroleum business and was largely absorbed by higher foreign taxes payable to governments of those foreign countries in which the Company's petroleum operations are located.

The percentage contribution of each of the Company's lines of business to consolidated net sales and revenues and earnings from operations for each of the years 1971 through 1975 is shown in the following table:

**Net Sales and Revenues**

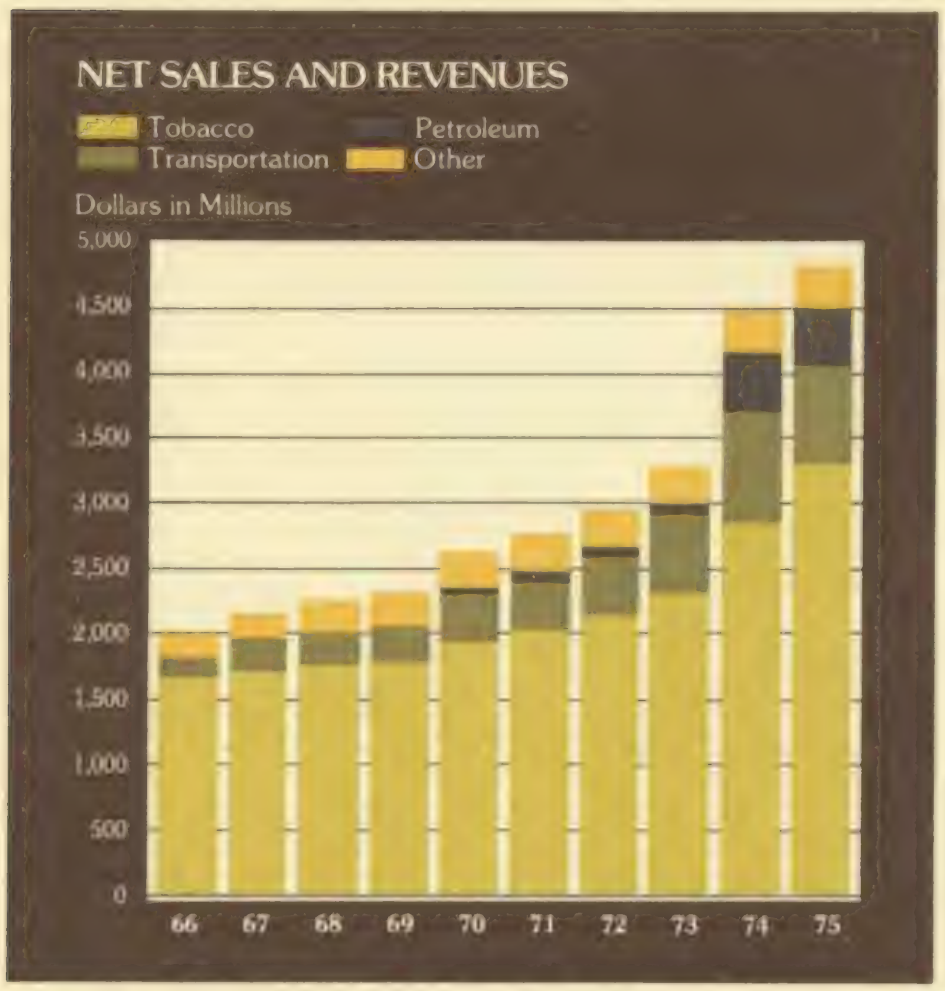
| | **1975** | 1974 | 1973 | 1972 | 1971 |
|---|---|---|---|---|---|
| Tobacco | **68.6**% | 64.3% | 71.3% | 73.3% | 74.8% |
| Transportation | **15.9** | 19.0 | 17.7 | 15.2 | 12.9 |
| Petroleum | **9.1** | 10.3 | 3.0 | 2.7 | 2.6 |
| Other | **6.4** | 6.4 | 8.0 | 8.8 | 9.7 |
| | **100.0**% | 100.0% | 100.0% | 100.0% | 100.0% |

**Earnings from Operations**

| | **1975** | 1974 | 1973 | 1972 | 1971 |
|---|---|---|---|---|---|
| Tobacco | **62.7**% | 50.0% | 82.6% | 82.8% | 87.7% |
| Transportation | **10.6** | 17.3 | 3.3 | 6.5 | 3.5 |
| Petroleum* | **23.1** | 30.8 | 9.9 | 7.3 | 5.0 |
| Other | **3.6** | 1.9 | 4.2 | 3.4 | 3.8 |
| | **100.0**% | 100.0% | 100.0% | 100.0% | 100.0% |

**Earnings from petroleum operations are subject to foreign income taxes at rates substantially greater than those applicable to the Company's non-petroleum businesses.*

The sales and revenues of the Company's non-tobacco businesses have grown from 25% of consolidated sales and revenues in 1971 to 31% in 1975. Earnings from operations from non-tobacco businesses have grown from 12% of consolidated earnings from operations in 1971 to 37% in 1975.




## Tobacco

Over the past five years tobacco sales and earnings from operations have increased at average annual compound rates of 11% and 6%, respectively.

Tobacco sales were $3.3 billion in 1975, up 15% over 1974's $2.9 billion. Price increases during 1974 and late in 1975 accounted for 8% of the gain and worldwide unit volume accounted for the remaining 7%. Tobacco earnings from operations rose to $528 million in 1975 from $413 million in 1974. The $115 million, or 28%, increase can be attributed to the price and unit volume increases, offset by higher costs, including increased advertising of $17 million and costs associated with developing and marketing new cigarette brands.

Tobacco sales for 1974 were $2.9 billion, up $546 million, or 23%, from the prior year. Approximately 75% of the 1974 gain was attributable to the acquisition of Macdonald Tobacco (effective January 1, 1974) and other worldwide unit volume gains. Tobacco earnings from operations declined to $413 million in 1974 from $434 million in 1973 primarily as a result of higher

operating costs, including a 23% rise in leaf tobacco prices during the 1974 leaf buying season. Since 1956, the Company has valued its tobacco inventories using the last-in, first-out (LIFO) method, thereby charging increased leaf tobacco costs against earnings immediately rather than deferring them to later years.

**Transportation**

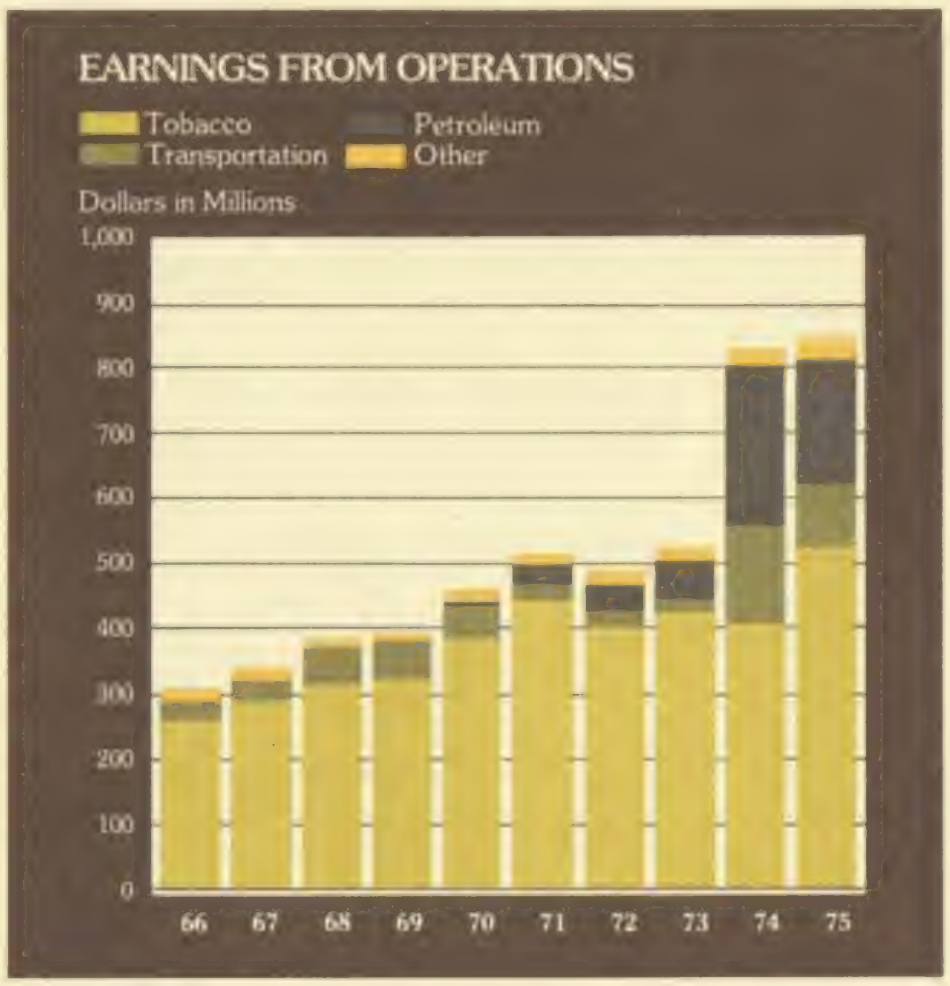
During 1975, transportation revenues were $768 million, a decrease of $87 million, or 10%, from 1974. Effective September 30, 1974, the Company sold its Puerto Rico service to the Puerto Rico Maritime Shipping Authority. The business sold contributed approximately $85 million to 1974 transportation revenues during the nine months prior to its sale. Also, volumes in the Company's continuing major trade routes in 1975 (primarily the North Atlantic) were significantly below the levels of mid-1974. The lower volumes were largely offset by improved rates and cargo mix the Company was able to obtain through the quality of its shipping service.

Transportation earnings from operations in 1975 were $90 million, down $53 million, or 37%, from 1974's $143 million. The decrease reflects both the loss of operating earnings from the discontinued business and increased operating costs of present operations. Lease expense for the year decreased $14 million but this was more than offset by increased depreciation expense associated with continuing operations. Substantially all of the reduction in lease expense resulted from the purchase early in 1975 of 24 vessels previously chartered by the Company under long-term leases. The Company believes it is well positioned to take maximum advantage of any upturn in world trade that may occur when international economic conditions improve.

Transportation revenues in 1974 reached $855 million, an increase of $272 million, or 47%, over 1973. Earnings from operations reached $143 million, an increase of $126 million over the prior year. Approximately two-thirds of the revenue increase can be attributed to the generally favorable world trade conditions existing in 1974, and improved rates on certain trade routes. The remainder of the increase resulted from the greater capacity of the expanded fleet. The 1974 earnings increase reflects the higher revenues, better operating performance, and lower redeployment and start-up costs compared with 1973. Principal cost increases during 1974 were bunker fuel, up $59 million; maintenance and repairs, up $18 million; lease expense, up $10 million; and depreciation of vessels and related equipment, up $11 million. These additional expenses reflect generally higher prices (especially with respect to bunker fuel, which quadrupled in price during 1974) and additional costs required to support the expanded level of operations in that year.

**Petroleum**

Sales by the petroleum business were $440 million in 1975, a decrease of $21 million, or 4.5%, from 1974. The sales decline resulted from a weak demand for oil during the year, especially during the fourth quarter. Sales during the fourth quarter of 1975 were $53 million less than in the comparable period of 1974. The weak fourth quarter followed a strong but temporary demand during the third quarter when sales were appreciably boosted in anticipation of price increases announced in October, 1975, by the Organization of Petroleum Exporting Countries (OPEC). Petroleum earnings from operations for 1975 were $195 million, down $59 million, or 23%, from the prior year. The reduced earnings reflect the lower 1975 revenues and higher operating



costs, including increased exploration costs related to the Company's search for new oil and gas reserves and increased royalty expenses of $15 million.

Petroleum sales and revenues reached $461 million in 1974, an increase of $361 million, and earnings from operations were $254 million, up $202 million over 1973. Almost all of the revenue and earnings from operations increases resulted from the quadrupling of posted prices announced by OPEC in late 1973. Petroleum earnings from operations are largely absorbed by taxes payable to the OPEC member states in which the Company's petroleum investments are located.

**Other Businesses**

Sales by the Company's other businesses (foods and aluminum products and packaging) increased in 1975 to $308 million, up $19 million, or 6.4%, over 1974 and earnings from operations were $30 million, up $15 million over the prior year. The increases in sales and earnings from operations resulted almost entirely from price increases during the last two years. Unit volumes for most products were below the levels of last year, reflecting the effect of prevailing economic conditions. Improved volumes for most products were evident during the fourth quarter.

Sales by these businesses during 1974 were $289 million, up $26 million, or 10%, over 1973 and earnings from operations declined to $15 million, down $7 million from the prior year. The sales increases resulted primarily from higher food prices and price and volume increases in the aluminum products and packaging businesses. The decline in 1974's earnings from operations was due in large part to the Company's adoption of the LIFO method for valuing certain inventories (principally aluminum and sugar) of these businesses which reduced earnings from operations by $15.6 million. The LIFO method was adopted to reflect currently the effect of increasing raw material prices on operating results.

Sales and revenues of the Company's other businesses declined in 1972 when compared to 1971 due to the sale in May, 1971, of the Company's corn processing business, Penick and Ford, Limited.

## INTEREST AND DEBT EXPENSE

Interest and debt expense was $55 million in 1975, $58 million in 1974, $41 million in 1973, and $30 million in 1972, reflecting several factors. The $3 million decline in 1975 results primarily from the repayment during the year of $29 million of ship mortgage bonds. The 1975 and 1974 amounts include full years' interest on the long-term ship mortgage bonds issued in conjunction with delivery of eight new SL-7 containerships late in 1972 and at various dates in 1973. Average short-term debt balances and effective borrowing rates were higher during the last two years than in 1973 and 1972 (effective rates were 7.7% in 1975 and 10% in 1974, compared to 6.5% and 5% in 1973 and 1972, respectively).

Between 1969 and 1973 the Company capitalized as SL-7 vessel cost the $28 million of construction loan interest and commitment fees, including $8 million in 1973 and $11 million in 1972.

## PROVISION FOR INCOME TAXES

The Company's provision for income taxes was 59% and 61% of earnings before taxes in 1975 and 1974, respectively, compared to 47% in 1973.

The higher rates of the last two years result from several factors, including higher taxes on petroleum earnings and the fact that petroleum earnings, which are taxed at rates considerably higher than the U.S. income tax rate, constituted a larger part of total earnings before taxes in 1975 and 1974 than in prior years.

In addition, investment tax credits in 1975 and 1974 amounted to only $7 million and $6 million, respectively, compared to $30 million in 1973. The Company uses the flow-through method of accounting for investment tax credits, whereby the provision for income taxes is reduced in the year the credit first becomes available. The high 1973 investment tax credit resulted primarily from expenditures for acquiring and equipping the SL-7 containerships.

Additional analysis of income taxes is contained in Note H to the financial statements.

## EXPANSION AND MODERNIZATION

Capital expenditures in 1975 were $175 million, compared to $126 million and $312 million in 1974 and 1973, respectively. Capital expenditures in the transportation business during 1975 were $74 million and included approximately $37 million for the purchase of 24 vessels previously chartered by the Company under long-term agreements.

During the past year, $73 million was expended in the tobacco business for expansion and modernization of existing facilities throughout the world.

During the last five years, capital expenditures have totaled $1 billion. No material amounts of debt or equity capital have been issued since 1973 to finance capital expenditures.

Capital expenditures are projected to be about $200 million for 1976. Of this amount, approximately 50% is expected to be spent for replacement and modernization in the tobacco business.

During 1975, the Company announced plans for its new World Headquarters, a half-million-square-foot office building to be located in Winston-Salem. The building is estimated to cost approximately $26 million and is scheduled for completion in the fall of 1977.

## CAPITAL EMPLOYED

Long-term debt (including current maturities) at year end amounted to $475 million. Repayments during 1975 totaled $38 million, including $29 million of ship mortgage bonds. The ship mortgage bonds are denominated in foreign currencies which have been translated at exchange rates in effect at December 31, 1975.

Short-term debt at year end was $110 million, $48 million less than the 1974 amount. The Company's total debt as a percentage of total capital decreased from 29% in 1974 to 24% at year-end 1975. Total debt as a percentage of total capital has averaged 28% for the last five years. If the net present value of financing leases were capitalized, the percentage of debt to total capital would have been 29% in 1975 and would have averaged 34% during the past five years. The Company feels that significant amounts of new debt could be incurred to finance business expansion without impairing present credit ratings.

The Company received $44 million upon the conversion of 1,996,077 shares of Preferred Stock during 1975, including 1,400,000 shares converted by underwriters to obtain common shares for resale to the public on behalf of two shareholders of the Company. The proceeds were added to the Company's general funds and were used for working capital and other corporate purposes.

## DIVIDENDS

The Company increased the quarterly dividend on the Common Stock from 72 cents to 77 cents per share for the fourth quarter of 1975. The Company's dividend payment per common share has increased each year for the past 22 years except for 1971, when dividend increases were prohibited by Federal economic guidelines.

For the past five years dividends per common share have averaged 49% of earnings per common share on a fully diluted basis. Dividends declared on the Common and Preferred Stocks during 1975 totaled $143 million, the highest for the Company's 76 consecutive years of dividend payments.

The Company has paid the regular dividend of 56.25 cents per share on its $2.25 Convertible Preferred Stock for each quarter since the issuance of that stock in May, 1969. The following table sets forth the dividends paid per share of Common Stock during 1975 and 1974:

| Quarter | 1975 | 1974 |
|---|---|---|
| First | $ .72 | $ .67 |
| Second | .72 | .67 |
| Third | .72 | .67 |
| Fourth | .77 | .72 |
| Year | $2.93 | $2.73 |

## STOCK PRICES

The high and low sales prices of the Common and Preferred Stocks on the New York Stock Exchange during the last two years were as follows:

| | Common | | | |
|---|---|---|---|---|
| | 1975 | | 1974 | |
| Quarter | High | Low | High | Low |
| First | 56¾ | 49½ | 49⅞ | 39¼ |
| Second | 60⅜ | 50½ | 48 | 39¾ |
| Third | 60 | 52⅛ | 46⅞ | 39¾ |
| Fourth | 61½ | 54¼ | 53⅜ | 37¼ |
| Year | 61½ | 49½ | 53⅜ | 37¼ |

| | Preferred | | | |
|---|---|---|---|---|
| | 1975 | | 1974 | |
| Quarter | High | Low | High | Low |
| First | 63 | 52½ | 52½ | 37¾ |
| Second | 68¼ | 55 | 49 | 40¼ |
| Third | 68 | 55¾ | 48⅛ | 37¾ |
| Fourth | 69½ | 60½ | 57¾ | 35¼ |
| Year | 69½ | 52½ | 57¾ | 35¼ |

# SELECTED FIVE-YEAR INFORMATION

Years Ended December 31 (Dollar Amounts in Thousands Except Per Share Statistics)

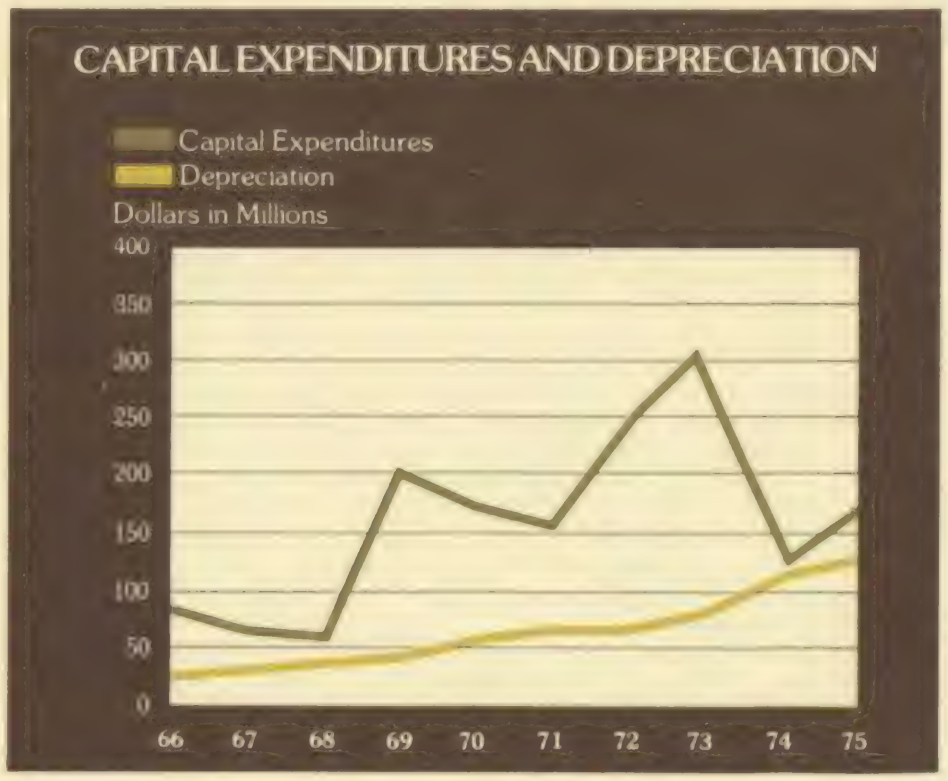
| | 1975 | 1974 | 1973 | 1972 | 1971 |
|---|---|---|---|---|---|
| Total current assets | **$1,697,354** | $1,558,991 | $1,146,228 | $1,144,349 | $1,059,459 |
| Total current liabilities | **713,681** | 735,484 | 426,505 | 464,313 | 311,832 |
| Working capital | **983,673** | 823,507 | 719,723 | 680,036 | 747,627 |
| Current assets/current liabilities | **2.4** | 2.1 | 2.7 | 2.5 | 3.4 |
| Net property, plant and equipment | **$1,215,367** | $1,150,931 | $1,160,472 | $ 934,984 | $ 751,126 |
| Total assets | **3,294,322** | 3,093,766 | 2,578,209 | 2,336,483 | 2,048,811 |
| Return on average total assets (1) | **11.5%** | 11.5% | 10.8% | 11.2% | 12.1% |
| Notes payable | **$ 109,648** | $ 157,683 | $ 46,926 | $ 12,455 | $ 17,416 |
| Long-term debt (including current maturities) | **474,907** | 525,175 | 568,476 | 538,119 | 470,787 |
| Stockholders' equity | **1,899,580** | 1,660,024 | 1,489,192 | 1,364,968 | 1,242,108 |
| Total capital | **2,484,135** | 2,342,882 | 2,104,594 | 1,915,542 | 1,730,311 |
| Return on average total capital (2) | **15.2%** | 14.8% | 13.9% | 14.4% | 14.9% |
| Capital expenditures | **$ 174,639** | $ 125,832 | $ 312,183 | $ 252,519 | $ 159,612 |
| Depreciation, depletion and amortization | **130,622** | 115,518 | 86,124 | 70,437 | 68,439 |
| Cash flow from operations | **488,673** | 469,783 | 398,319 | 345,586 | 323,778 |
| Dividends on Common and Preferred Stocks | **$ 142,902** | $ 130,964 | $ 126,833 | $ 120,304 | $ 115,636 |
| Dividends per common share | **2.93** | 2.73 | 2.636 | 2.496 | 2.40 |
| Dividend payout ratio (3) | **44%** | 46% | 53% | 54% | 53% |
| Common Stock price range—High | **61½** | 53⅜ | 55¾ | 78 | 69½ |
| Low | **49½** | 37¼ | 36½ | 47¾ | 50¼ |
| Net earnings as a percent of net sales and revenues | **7.0%** | 6.6% | 7.5% | 7.8% | 8.0% |
| Return on average common stockholders' equity | **19.0%** | 18.7% | 17.0% | 17.5% | 18.8% |
| Book value per common share | **$40.68** | $37.40 | $33.59 | $30.77 | $28.21 |
| Number of stockholders at year end | **121,398** | 125,176 | 124,371 | 120,321 | 126,790 |
| Number of employees at year end | **34,666** | 32,454 | 31,477 | 30,042 | 29,484 |

Information for 1974 and prior years has been restated to reflect a change in method of accounting for foreign currency translation. See Note A to the financial statements.

(1) Net earnings plus after-tax interest and debt expense divided by average total assets.

(2) Net earnings plus after-tax interest and debt expense divided by average total capital; excluding vessel construction loans. (Total capital is the sum of stockholders'equity, short-term notes payable, and total long-term debt.)

(3) Dividends per share as a percentage of earnings per common share on a fully diluted basis.



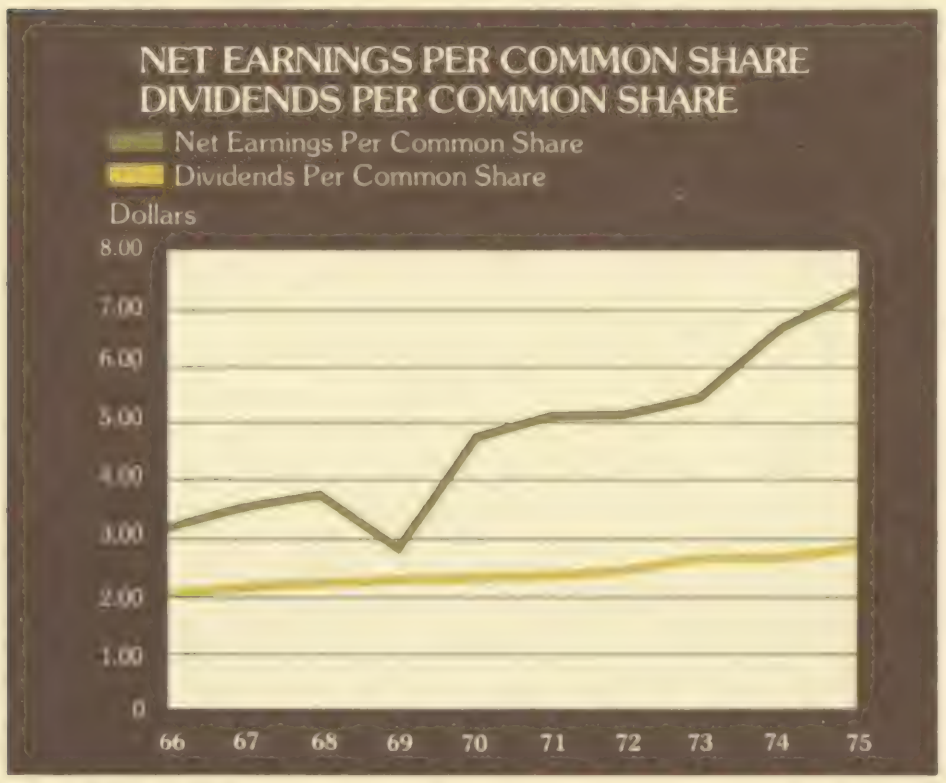
R.J.REYNOLDS INDUSTRIES, INC.

# CONSOLIDATED STATEMENTS OF EARNINGS AND EARNINGS RETAINED

For the Years Ended December 31 (Dollars in Thousands Except Per Share Statistics)

| | 1975 | 1974 (Note A) |
|---|---|---|
| **Net sales and revenues** | **$4,837,643** | $4,500,909 |
| **Costs and expenses:** | | |
| Cost of products sold and operating expenses | **3,432,305** | 3,197,804 |
| Selling, advertising, administrative and general expenses | **562,867** | 477,877 |
| **Earnings from operations** | **842,471** | 825,228 |
| Interest and debt expense | **54,465** | 57,598 |
| Foreign currency (gains) losses | **(15,514)** | 28,590 |
| Other (income) expense, net | **(13,720)** | (14,246) |
| **Earnings before provision for income taxes** | **817,240** | 753,286 |
| Provision for income taxes | **478,567** | 456,383 |
| **Net earnings** | **338,673** | 296,903 |
| Dividends on $2.25 Convertible Preferred Stock | **12,129** | 15,772 |
| **Net earnings applicable to Common Stock** | **326,544** | 281,131 |
| **Earnings retained at beginning of year** | **1,324,539** | 1,158,600 |
| **Deduct:** | | |
| Cash dividends on Common Stock | **130,773** | 115,192 |
| Charges related to stock options exercised | **128** | — |
| **Earnings retained at end of year** | **$1,520,182** | $1,324,539 |
| **Net earnings per common share:** | | |
| Primary | **$7.39** | $6.66 |
| Fully diluted | **6.71** | 5.97 |
| **Average number of common shares outstanding:** | | |
| Primary | **44,183,793** | 42,188,574 |
| Fully diluted | **50,473,159** | 49,765,082 |

See Notes to Consolidated Financial Statements.



R.J.REYNOLDS INDUSTRIES, INC.

# CONSOLIDATED BALANCE SHEETS

December 31 (Dollars in Thousands)

| | 1975 | 1974 |
|---|---|---|
| **ASSETS** | | (Note A) |
| **Current assets:** | | |
| Cash and short-term investments | $ 35,244 | $ 42,696 |
| Accounts and notes receivable (less allowances of $17,426 and $15,043, respectively) | 379,633 | 367,085 |
| Inventories | 1,269,249 | 1,134,771 |
| Prepaid expenses | 13,228 | 14,439 |
| Total current assets | 1,697,354 | 1,558,991 |
| **Property, plant and equipment—at cost** | 1,909,638 | 1,783,989 |
| Less allowances for depreciation, depletion and amortization | 694,271 | 633,058 |
| Net property, plant and equipment | 1,215,367 | 1,150,931 |
| **Cost in excess of net assets of businesses acquired** | 171,346 | 174,224 |
| **Other assets and deferred charges** | 210,255 | 209,620 |
| | $3,294,322 | $3,093,766 |
| **LIABILITIES AND STOCKHOLDERS' EQUITY** | | |
| **Current liabilities:** | | |
| Notes payable | $ 109,648 | $ 157,683 |
| Accounts payable and accrued accounts | 347,597 | 296,057 |
| Current maturities of long-term debt | 39,581 | 37,951 |
| Income taxes accrued | 216,855 | 243,793 |
| Total current liabilities | 713,681 | 735,484 |
| **Long-term debt (less current maturities)** | 435,326 | 487,224 |
| **Other non-current liabilities** | 51,473 | 73,809 |
| **Deferred income taxes** | 194,262 | 137,225 |
| **Stockholders' equity:** | | |
| Preferred Stock | 51,246 | 72,345 |
| Common Stock | 227,204 | 212,234 |
| Paid-in capital | 100,948 | 50,906 |
| Earnings retained | 1,520,182 | 1,324,539 |
| Total stockholders' equity | 1,899,580 | 1,660,024 |
| | $3,294,322 | $3,093,766 |

See Notes to Consolidated Financial Statements.

R.J.REYNOLDS INDUSTRIES, INC.

# CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION

For the Years Ended December 31 (Dollars in Thousands)

| | 1975 | 1974 |
|---|---|---|
| | | (Note A) |
| **Working capital was provided by:** | | |
| Operations: | | |
| Net earnings | **$338,673** | $296,903 |
| Depreciation, depletion and amortization | **130,622** | 115,518 |
| Deferred income taxes | **57,037** | 11,306 |
| Long-term foreign currency translation (gains) losses | **(16,760)** | 23,166 |
| Other | **(20,899)** | 22,890 |
| Total from operations | **488,673** | 469,783 |
| Proceeds from long-term debt | **5,910** | 16,441 |
| Proceeds from issuance of Company's stocks | **67,975** | 7,244 |
| Net decrease in long-term assets from sale of certain transportation operations | **—** | 9,841 |
| Other disposals of property, plant and equipment | **16,082** | 4,289 |
| | **578,640** | 507,598 |
| **Working capital was used for:** | | |
| Capital expenditures | **174,639** | 125,832 |
| Cash dividends | **142,902** | 130,964 |
| Long-term debt becoming currently payable | **41,404** | 40,677 |
| Retirement of Preferred Stock upon conversion | **21,099** | 2,351 |
| Net increase in long-term assets from acquisitions accounted for as purchases | **18,584** | 49,046 |
| Cost of treasury shares purchased | **3,091** | — |
| Other (principally other assets and deferred charges) | **16,755** | 54,944 |
| | **418,474** | 403,814 |
| Increase in working capital | **$160,166** | $103,784 |
| **Analysis of changes in working capital:** | | |
| Increase (decrease) in current assets: | | |
| Cash and short-term investments | **$ (7,452)** | $ 3,000 |
| Accounts and notes receivable | **12,548** | 107,731 |
| Inventories | **134,478** | 299,453 |
| Prepaid expenses | **(1,211)** | 2,579 |
| Decrease (increase) in current liabilities: | | |
| Notes payable | **48,035** | (110,757) |
| Accounts payable and accrued accounts | **(51,540)** | (77,732) |
| Current maturities of long-term debt | **(1,630)** | 46,952 |
| Income taxes accrued | **26,938** | (167,442) |
| **Increase in working capital** | **$160,166** | $103,784 |

See Notes to Consolidated Financial Statements.

# NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## NOTE A
## SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### Consolidation
The Company includes in its consolidated financial statements the accounts of the parent and all subsidiaries.

### Change in Method of Accounting for Foreign Currency Translation
During 1975 the Company changed its method of accounting for foreign currency translation in conformity with the requirements of Statement No. 8 published by the Financial Accounting Standards Board in October, 1975. All prior periods have been restated to reflect this change, which generally requires that cash and amounts owed by or to an enterprise that are denominated in foreign currencies must be translated at exchange rates in effect on the balance sheet date. Inventories, properties and other non-monetary assets and liabilities must be translated at the exchange rates in effect on the dates the related assets were acquired or the liabilities incurred. Under the new method, translation gains and losses are recognized in earnings in the period the exchange rate changes.

Prior to 1975, differences between the recorded U.S. dollar amounts of short-term foreign currency vessel construction loans and the amounts obtained by applying year-end exchange rates to such loans were capitalized in vessel construction accounts. Long-term assets and liabilities were translated at historical exchange rates, thereby recognizing foreign currency gains and losses associated with long-term receivables and payables only when realized in cash. Net cumulative translation gains were deferred.

The effect of adopting this method was to increase 1975 earnings from operations and net earnings by $1.4 million and $11 million, respectively, and primary and fully diluted net earnings per common share by 24 cents and 21 cents, respectively. The impact of retroactive application of the new method to 1974 was to increase that year's earnings from operations by $1.4 million, decrease net earnings by $14 million, and decrease primary and fully diluted net earnings per common share by 33 cents and 27 cents, respectively. The previously reported balance of earnings retained at January 1, 1974, was decreased by $23 million. Foreign currency gains and losses, including translation gains and losses, are set forth separately in the statement of earnings.

### Inventories
Inventories, principally leaf tobacco, but including supplies and manufactured products, are stated at cost (most of which are valued using the LIFO method).

The current replacement value of inventories at December 31, 1975 and 1974, was approximately $581 and $488 million, respectively, greater than the amount at which these inventories were carried on the balance sheets.

### Interest Expense
The Company capitalized as vessel cost the $28 million of construction loan interest and commitment fees incurred during the five-year construction period (1969 to 1973) of the SL-7 containerships.

### Investment Tax Credit
The Company uses the flow-through method in accounting for investment tax credits, whereby the provision for income taxes is reduced in the year the tax credits first become available, rather than deferring the credit over the life of the related asset.

### Earnings Per Share
Primary earnings per share are determined by dividing net earnings applicable to Common Stock by the average number of common shares and equivalent common shares outstanding.

Fully diluted earnings per share are calculated using the "treasury stock" method. This method assumes that all shares of the Convertible Preferred Stock outstanding during the year were converted into Common Stock and the conversion proceeds used to purchase treasury common shares at the higher of the average daily price or year-end closing price of the Common Stock.

### Other Policies
Sales of products are recognized in income as customer shipments are made. Net sales include Federal and foreign excise taxes on tobacco products of $1,309 million in 1975 and $1,201 million in 1974. The Company's transportation revenues and related vessel voyage expenses are generally recognized at the commencement of a voyage.

The excess of cost over net assets of businesses acquired subsequent to October 31, 1970, is being amortized over periods not exceeding 40 years. Generally, amounts recorded prior to that date are not being amortized since the Company believes no permanent impairment of the value of these assets has occurred.

The Company includes in other (income) expense, net, items of a financial nature, principally interest income.

## NOTE B
## PROPERTY, PLANT AND EQUIPMENT

Components of property, plant and equipment at December 31 are shown in the chart on the right.

The Company depreciates assets used in the transportation and petroleum businesses using the straight-line method. For all other assets, depreciation is determined principally by accelerated methods. Renewals, conversions or betterments which add materially to the value or useful lives are charged to property, plant and equipment accounts.

| | (Dollars in Thousands) | |
|---|---|---|
| | **1975** | 1974 |
| | | (Note A) |
| Land and land improvements | **$ 23,432** | $ 19,099 |
| Buildings and leasehold improvements | **204,775** | 185,434 |
| Machinery and equipment | **425,396** | 365,939 |
| Vessels, containers, and other marine equipment | **1,128,514** | 1,072,174 |
| Petroleum-producing properties | **76,030** | 95,992 |
| Construction-in-process | **51,491** | 45,351 |
| | **1,909,638** | 1,783,989 |
| Less accumulated allowances for depreciation, depletion and amortization | **694,271** | 633,058 |
| Net property, plant and equipment | **$1,215,367** | $1,150,931 |

## NOTE C LONG-TERM DEBT

| | (Dollars in Thousands) | | | |
|---|---|---|---|---|
| | **December 31, 1975** | | December 31, 1974 | |
| | | | (Note A) | |
| | **Due Within One Year** | **Due After One Year** | Due Within One Year | Due After One Year |
| **Long-term debt consists of the following:** | | | | |
| 7½% Ship Mortgage Bonds, payable in Deutschemarks with semi-annual sinking fund payments through1987 | **$13,984** | **$145,350** | $15,133 | $172,425 |
| 8½% and 8¾% Ship Mortgage Bonds, payable in Dutch Guilders with semi-annual sinking fund payments through 1981 | **12,733** | **57,233** | 13,609 | 74,780 |
| 7⅞% Debentures, due February 1, 2001, with annual sinking fund payments beginning in 1982 | — | **100,000** | — | 100,000 |
| 7⅞% Debentures, due September 1, 1994, with annual sinking fund payments beginning in 1975 (reduced by $1,778 and $6,778 of such Debentures held by the Company on December 31, 1975 and 1974, respectively, for future sinking fund requirements) | **3,222** | **90,000** | — | 93,222 |
| 7% Subordinated Debentures, due June 1, 1989, with annual sinking fund payments beginning in 1980 | — | **15,849** | — | 15,849 |
| Other indebtedness with various interest rates and maturities | **9,642** | **26,894** | 9,209 | 30,948 |
| | **$39,581** | **$435,326** | $37,951 | $487,224 |

The payment schedule of debt due after one year is as follows (dollars in thousands): 1977—$35,808; 1978—$33,912; 1979—$34,444; 1980—$37,245; 1981 and later—$293,917.

## NOTE D
## COMMITMENTS AND CONTINGENCIES

Three civil actions purporting to be class actions, two of which were brought in July, 1974, and one of which was brought in April, 1975, are pending against the six major United States cigarette manufacturers, including the Company, and others in which certain tobacco farmers allege violations of the antitrust laws and seek damages of approximately $2.2 billion, $336 million, and an unspecified amount, respectively, plus attorneys' fees and costs. In one of the cases, the Trial Court held in September, 1975, that the action was not a proper class action but the decision has been appealed. Counsel has advised the Company that in its opinion none of these cases is a proper class action, in which event none of the cases should result in any material liability. Investigation of the merits of the three cases is not complete. However, counsel has advised the Company, based on its investigation and the formal discovery to date, that in its opinion the Company has substantial factual and legal defenses on the merits to the charges made. Accordingly, the Company has made no provision for this matter in its financial statements.

The Company and its subsidiaries are involved in certain other litigation, renegotiation, and customs matters which in the aggregate are not expected to have any material adverse effect on the Company's financial statements.

The Company had various capital spending commitments of $50 million at December 31, 1975. For additional information concerning commitments and contingencies, see Notes E, F and H.

## NOTE E
## UNITED STATES LINES, INC.

In 1970, a merger agreement was entered into with Walter Kidde and Company, Inc. and United States Lines, Inc. under which Reynolds was to acquire, subject to the approvals of the Federal Maritime Commission and the Interstate Commerce Commission, all of the common stock of United States Lines in exchange for a $65 million promissory note payable to Kidde. Interest on the note was to accrue from November 9, 1970, at 8% and unpaid installments of interest were to bear interest at 6%. During 1974, the Federal Maritime Commission approved the merger agreement, subject to certain conditions, but the Commission's decision was vacated during 1974 by an United States Court of Appeals, and the United States Supreme Court declined to review the Court of Appeals decision. The Interstate Commerce Commission has not yet rendered its final decision on the proposed acquisition.

On November 9, 1975, the right of Reynolds to acquire United States Lines under the merger agreement expired because approvals of the Federal Maritime Commission and the Interstate Commerce Commission had not been obtained and Reynolds became obligated under a supplemental agreement (the consummation of which is barred by a court order as noted below) with Kidde entered into concurrently with the merger agreement to deposit with an escrow agent the note described in the merger agreement for $65 million plus interest and to designate a financial institution to cause an alternative disposition of the stock or assets of United States Lines to be made no later than November 9, 1976. The supplemental agreement provides that Reynolds will receive any excess of the amount realized upon such disposition over the agreed consideration of $65 million plus interest, and that Reynolds will make up any deficiency between the amount so realized and the agreed consideration of $65 million plus interest.

Pursuant to a preliminary injunction entered in 1971 by an United States District Court in an antitrust suit brought by the Department of Justice in 1970, the Company is prohibited from consummating the merger agreement or the supplemental agreement pending further order of the Court. In December, 1975, the Court entered an order modifying the 1971 preliminary injunction so as to permit the designation of a financial institution and its entering into communications with prospective purchasers and others concerning the disposition of United States Lines, and in December, 1975, a financial institution was so designated. The Department of Justice has asked the Court to reconsider and vacate its order permitting the designation of a financial institution under the supplemental

agreement. Except as modified by the December, 1975, order, the 1971 preliminary injunction remains in effect and unless further modified prohibits the consummation of the supplemental agreement. Accordingly, the note for $65 million plus interest has not been placed in escrow and the Company's financial statements do not reflect the $65 million note or interest thereon. If an alternative disposition in accordance with the supplemental agreement is ultimately permitted by the Court, the Company would incur a loss if such disposition is made for a consideration below the equivalent of the $65 million note and interest thereon.

The Company is unable to predict the outcome of the foregoing matters and the effect, if any, upon the Company's financial statements.

An antitrust action was brought by a competitor in 1969 alleging violations of the antitrust laws and seeking to enjoin a time charter and lease then proposed but no longer pending for the charter of the containership fleet of United States Lines to Sea-Land Service, Inc. At the same time, the competitor requested that Reynolds be required to divest itself of McLean Industries, Inc., the parent of Sea-Land, and that Kidde be required to divest itself of United States Lines. In the opinion of counsel, this suit is without merit as to Reynolds, McLean and Sea-Land.

## NOTE F
## LEASES AND CHARTERS

Leases and charters for vessels and related equipment and facilities are used extensively in connection with the transportation business. Leases for major equipment and facilities have remaining terms ranging from two to 25 years. Lease expense was as follows:

| | (Dollars in Thousands) | |
|---|---|---|
| | **1975** | 1974 |
| **Noncancelable** | | |
| Non-financing leases | **$20,425** | $18,170 |
| Financing leases | **27,396** | 37,642 |
| Total | **47,821** | 55,812 |
| **Cancelable leases** | **30,746** | 33,989 |
| Total lease expense | **$78,567** | $89,801 |

At December 31, 1975, the Company was obligated under noncancelable lease agreements to make minimum payments in future years as follows:

| | (Dollars in Thousands) | | |
|---|---|---|---|
| | Non-Financing | Financing | Total |
| 1976 | $22,780 | $ 24,692 | $ 47,472 |
| 1977 | 15,440 | 24,532 | 39,972 |
| 1978 | 11,533 | 24,457 | 35,990 |
| 1979 | 10,474 | 24,334 | 34,808 |
| 1980 | 7,723 | 23,609 | 31,332 |
| 1981-1985 | 22,615 | 108,208 | 130,823 |
| 1986-1990 | 7,728 | 82,540 | 90,268 |
| 1991-1995 | 3,437 | 60,998 | 64,435 |
| Remainder | 28 | 35,683 | 35,711 |

The net present values of the Company's future minimum lease obligations under financing leases at December 31, 1975 and 1974, are shown below by type of property along with the weighted average and range of interest rates specified or implicit in the leases.

| | (Dollars in Thousands) | | | |
|---|---|---|---|---|
| | **1975 Interest Rates** | | **Present Value Amounts** | |
| | Weighted Average | Range | **1975** | 1974 |
| Land and buildings | 7% | 3%-9% | **$107,610** | $111,794 |
| Other property, plant and equipment | 7% | 3%-17% | **106,322** | 176,119 |
| | | | **$213,932** | $287,913 |

If all noncancelable financing leases were capitalized, there would be no material effect on net earnings. Substantially all of the decline in 1975 lease expense and present value amounts, compared to 1974, resulted from the Company's purchase, early in 1975, of 24 vessels previously chartered by the Company under long-term leases.

## NOTE G
## CAPITAL CHANGES AND RELATED MATTERS

| | (Dollars in Thousands) | |
|---|---|---|
| | **1975** | 1974 |
| **$2.25 Convertible Preferred Stock —without par value** ($10.57 stated value): Authorized 4,860,235 shares and 6,856,312 shares at December 31, 1975 and 1974, respectively; outstanding 4,848,285 shares and 6,844,362 shares at December 31, 1975 and 1974, respectively. | | |
| Balance at beginning of year | **$ 72,345** | $ 74,696 |
| Shares converted into Common Stock (1,996,077 shares in 1975 and 222,397 shares in 1974) | **(21,099)** | (2,351) |
| Balance at end of year | **$ 51,246** | $ 72,345 |
| **Common Stock —par $5:** Authorized 60,000,000 shares; outstanding 45,440,835 shares and 42,446,722 shares at December 31, 1975 and 1974, respectively. | | |
| Balance at beginning of year | **$212,234** | $210,565 |
| Shares issued upon conversion of Preferred Stock (2,994,113 shares in 1975 and 333,595 shares in 1974) | **14,970** | 1,669 |
| Balance at end of year | **$227,204** | $212,234 |
| **Treasury Common Stock** | | |
| Balance at beginning of year | **—** | — |
| Purchased (53,550 shares) | **$ 3,091** | — |
| Delivered in connection with acquisition of a business (44,000 shares) | **(2,548)** | — |
| Sales upon exercise of stock options (9,550 shares) | **(415)** | — |
| Amount charged to earnings retained (difference between option price and cost of treasury stock) | **(128)** | — |
| Balance at end of year | **$ —0—** | — |
| **Paid-in capital** | | |
| Balance at beginning of year | **$ 50,906** | $ 45,331 |
| Net proceeds from conversion of Preferred Stock into Common Stock | **50,042** | 5,575 |
| Balance at end of year | **$100,948** | $ 50,906 |

Each share of the Preferred Stock is convertible into 1.5 shares of the Company's Common Stock on surrender of the preferred share and payment of $22 in cash. Upon conversion the cash proceeds and the stated value of the converted preferred shares less the par value of the common shares issued is credited to paid-in capital. The Company may call for redemption of the Preferred Stock after June 30, 1979, at $50 per share (aggregating $242 million at December 31, 1975) plus accrued dividends to the redemption date. In the event of involuntary liquidation, holders of the Preferred Stock are entitled to $10.57 per share plus accrued dividends. Of the authorized but unissued common shares at December 31, 1975, 7,272,428 were reserved for conversion of 4,848,285 shares of preferred shares issued.

The Career Executive Stock Plan, approved by the stockholders at the 1974 annual meeting, provides for the granting of options to certain officers and employees. The maximum number of shares of the Company's Common Stock which may be purchased under the plan is 600,000 and individual purchases are limited to 30,000 shares.

The plan permits the granting of both qualified and non-qualified options (as defined under the Internal Revenue Code) which may run for periods of up to five years as to qualified and up to ten years as to non-qualified options. However, no option may be exercised prior to one year after the date of grant. The option price is the average quoted market price on the date of grant. Options granted that lapse or are canceled prior to exercise are added back to the shares authorized for future options.

In 1975, 105,700 qualified and 97,200 non-qualified options were granted at an average option price of $57.97. In 1974, 47,050 qualified and 75,450 non-qualified options were granted at an average option price of $43.44.

During 1975, 4,650 options (900 of which were granted in 1975) were canceled and 9,550 were exercised. To satisfy the exercise of options, the Company purchased on the open market and reissued to optionees 9,550 shares of Common Stock at an average cost of $56.83 per share. As of December 31, 1975, 279,250 shares of the Company's Common Stock were reserved for future grants.

## NOTE H
## PROVISION FOR INCOME TAXES

The provision for income taxes consists of the following:

| | (Dollars in Thousands) | |
|---|---|---|
| | **1975** | 1974 |
| | | (Note A) |
| **Current:** | | |
| Federal | **$203,298** | $192,171 |
| State | **26,646** | 22,693 |
| Foreign | **191,586** | 230,213 |
| Total | **421,530** | 445,077 |
| **Deferred:** | | |
| Federal | **59,003** | 10,519 |
| State | **1,287** | 269 |
| Foreign | **(3,253)** | 518 |
| Total | **57,037** | 11,306 |
| Total provision for income taxes | **$478,567** | $456,383 |

Deferred income tax expense results from timing differences in the recognition of revenue and expense for book and tax purposes. The sources of these differences and the tax effect of each were as follows:

| | (Dollars in Thousands) | |
|---|---|---|
| | **1975** | 1974 |
| | | (Note A) |
| Excess of tax over book depreciation | **$29,277** | $ 15,898 |
| Unrealized foreign currency gains (losses) | **11,584** | (12,268) |
| Various other items | **16,176** | 7,676 |
| Deferred income taxes | **$57,037** | $ 11,306 |

The effective tax rate was 58.6% in 1975 and 60.6% in 1974. The differences between the amounts recorded

and the amounts computed by applying the Federal income tax rate of 48% to earnings before provision for income taxes are explained as follows:

| | (Dollars in Thousands) | | | |
|---|---|---|---|---|
| | **1975** | | 1974 (Note A) | |
| | **Amount** | **% of Pre-tax Income** | Amount | % of Pre-tax Income |
| Income tax computed at statutory U.S. Federal income tax rate | **$392,275** | **48.0%** | $361,577 | 48.0% |
| Taxes on foreign operations in excess of statutory U.S. Federal income tax rate | **71,218** | **8.7** | 79,823 | 10.6 |
| State taxes, net of Federal benefit | **14,525** | **1.8** | 11,940 | 1.6 |
| Investment tax credit | **(6,935)** | **(0.8)** | (5,716) | (0.8) |
| Miscellaneous items | **7,484** | **0.9** | 8,759 | 1.2 |
| Provision for income taxes | **$478,567** | **58.6%** | $456,383 | 60.6% |

No provision has been made for U.S. income taxes (not material in amount) that would be payable upon remittance of earnings retained abroad by foreign subsidiaries, since it is the Company's intention to reinvest these earnings abroad.

The Government of Kuwait has informed the Company that it wishes to meet in late February, 1976, to review the relationship between the Government and the Company. The Company understands that the Government seeks to increase the level of payments by the Company to the Government. While the effect of any agreement which may result from these discussions cannot be determined at this time, management believes that any such agreement will not have a material effect on these financial statements.

There are a number of issues pending as a result of Internal Revenue Service audits, which are not expected to have a material effect on the Company's financial statements.

## NOTE I
## PENSION PLANS

The Company provides retirement benefits for substantially all of its regular full-time employees through Company-administered plans and plans administered by labor unions under collective bargaining agreements. The Company's policy with respect to Company-administered plans is to fund pension costs accrued.

The total expense for the Company-administered plans increased from $21 million in 1974 to $28 million in 1975, primarily as a result of increased payrolls.

The assets of the Company-administered plans exceeded the actuarially computed value of vested benefits according to the most recent actuarial valuations.

In order to comply with the provisions of the Employee Retirement Income Security Act of 1974, the Company-administered plans have been amended, effective January 1, 1976, to provide for full vesting after ten years of credited service. Had this change been effective for 1975, pension expense would have increased by approximately $2.7 million, according to actuarial estimates, and certain plans would have had total actuarially computed value of vested benefits in excess of assets by $22 million at the most recent valuation date.

The Company makes payments under the terms of various collective bargaining agreements to provide welfare benefits, including pension benefits, for employees covered under such agreements.

## NOTE J
## ACQUISITIONS AND SALE OF PROPERTIES

During the two years ended December 31, 1975, the Company purchased certain businesses and sold certain transportation operations. The net effects of these transactions are included in the Consolidated Statements of Changes in Financial Position. The following table provides additional detail regarding these transactions:

| | (Dollars in Thousands) | |
|---|---|---|
| | **1975** | 1974 |
| **Sale of certain transportation operations:** | | |
| Property, plant and equipment | — | $61,764 |
| Cost in excess of assets previously acquired assigned to assets sold | — | 15,000 |
| Long-term portion of notes received in exchange | — | (66,923) |
| Net decrease in long-term assets | — | $ 9,841 |
| **Acquisitions accounted for as purchases:** | | |
| Property, plant and equipment | **$16,462** | $22,628 |
| Other assets | **24,138** | 92,231 |
| Liabilities assumed | **(734)** | (64,350) |
| Cost in excess of net assets of businesses acquired | **2,163** | 24,136 |
| Total cost of acquisitions | **42,029** | 74,645 |
| Less working capital at dates of acquisition | **23,445** | 25,599 |
| Net increase in long-term assets | **$18,584** | $49,046 |

## NOTE K
## FOREIGN OPERATIONS

The Company's operations in foreign countries are summarized as follows:

| | (Dollars in Thousands) | |
|---|---|---|
| | **1975** | 1974 |
| | | (Note A) |
| Assets | **$ 590,238** | $ 490,422 |
| Liabilities | **337,378** | 373,332 |
| Net sales and revenues | **1,324,056** | 1,201,943 |
| Earnings from operations | **217,227** | 270,265 |
| Net earnings | **40,795** | 62,333 |

In addition, most of the Company's transportation operations are dependent on foreign trade, and approximately 10% of the sales of tobacco products in 1975 resulted from exports.

# REPORT OF INDEPENDENT ACCOUNTANTS

ERNST & ERNST
2015 Wachovia Building
Winston-Salem, North Carolina

R.J.Reynolds Industries, Inc.
Its Directors and Stockholders

We have examined the consolidated balance sheets of R.J.Reynolds Industries, Inc. and subsidiaries as of December 31, 1975 and 1974, and the related consolidated statements of earnings and earnings retained and changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

As explained in Note E to the financial statements, the right of the Company to acquire United States Lines, Inc. under the merger agreement expired on November 9, 1975. Upon expiration, the Company became obligated under a supplemental agreement, the consummation of which is barred by a court order, to deposit with an escrow agent the note described in the merger agreement for $65,000,000 plus interest and to designate a financial institution to cause an alternative disposition of the stock or assets of United States Lines to be made no later than November 9, 1976. Since the consummation of the supplemental agreement is barred by the court order, the financial statements do not reflect the $65,000,000 note or accrued interest thereon. The Company is unable to predict the outcome of this matter and the effect, if any, upon the financial statements.

In our opinion, subject to the effects, if any, of the ultimate resolution of the matter discussed in the preceding paragraph, the financial statements referred to above present fairly the consolidated financial position of R.J.Reynolds Industries, Inc. and subsidiaries at December 31, 1975 and 1974, and the consolidated results of their operations and the changes in their consolidated financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis after restatement for the change, with which we concur, in the method of accounting for foreign currency translation as described in Note A to the financial statements.

Ernst & Ernst

February 12, 1976

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Verenigde Machinefabrieken N.V.,
Holland

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CHAS. B. WADE, JR. (Secretary)
Senior Vice President,
R.J.Reynolds Industries, Inc.

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Retired Manager, Leaf Buying,
R.J.Reynolds Tobacco Company

S. A. ANGOTTI
Retired Senior Vice President,
R.J.Reynolds Industries, Inc.

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Former Partner,
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R. G. VALLANDINGHAM
Retired Superintendent of Leaf Buying,
R.J.Reynolds Tobacco Company

JOHN C. WHITAKER
Retired Chairman,
R.J.Reynolds Tobacco Company

[1] Member, Audit Committee.
[2] Chairman, Audit Committee.
[3] Elected January 15, 1976.
[4] Effective March 1, 1976.

**Registrar**
MANUFACTURERS HANOVER TRUST COMPANY
Corporate Trust Division
4 New York Plaza
New York, New York 10015

**Transfer Agents**
THE CHASE MANHATTAN BANK, N.A.
1 New York Plaza, 14th Floor
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New York, New York 10015

**Stockholder Inquiries**
Communications concerning transfer requirements and lost certificates should be directed to either Transfer Agent. Communications concerning dividends and change of address should be directed to R.J.Reynolds Industries, Inc., Shareholder Services Department, Box 2959, Winston-Salem, North Carolina 27102.

**Common and Preferred Shares**
Listed on the New York Stock Exchange (trading symbol: RJR).

**Corporate Headquarters**
Reynolds Building
Fourth & Main Streets
Winston-Salem, North Carolina
27102
Telephone: (919) 748-4000

**Proxy Statement and Proxy**
A formal notice of the Annual Meeting, together with Proxy Statement and Proxy, will be mailed in March to stockholders of record at the close of business March 2, 1976.

**Availability of Form 10-K**
On or after March 31, 1976, a copy of the Company's Annual Report to the Securities and Exchange Commission on Form 10-K for the year ended December 31, 1975, will be provided to stockholders upon written request to the Secretary, R.J.Reynolds Industries, Inc., Winston-Salem, North Carolina 27102.

R.J.Reynolds Industries, Inc.

Winston-Salem, N. C. 27102